ST 97-28
Tax Type: SALES TAX
Issue: International Fuel Usage (Exemption Claimed)
Use Tax on Purchases, Fixed Assets, or Consumables

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE	)	Case No.
OF THE STATE OF ILLINOIS,	)	Reg. No.
v.	)	NTL Nos.
	)	
TAXPAYER,	)	John E. White,
Taxpayer.	)	Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Michael Koenigsknecht and John Roach, Gardner Carton & Douglas, for TAXPAYER. Mark Dyckman, for the Illinois Department of Revenue.

Synopsis:

The Illinois Department of Revenue ("Department") issued two Notices of Tax Liability ("NTL's") to TAXPAYER ("TAXPAYER" or "taxpayer") following an audit of TAXPAYER's business. NTL no. XXXXX was issued regarding the period beginning 1/1/91 through 11/30/93, and NTL no. XXXXX was issued regarding the period beginning 12/1/93 through 12/31/93. A large portion of the tax identified in the NTL's was Illinois use tax assessed on TAXPAYER's purchases of aircraft fuel during the audit periods. TAXPAYER protested the NTL's and requested a hearing.

In a pre-hearing order, the parties agreed to limit the issues presented for resolution. The parties agreed the taxability issue could be stated in the alternative, to wit:

> Whether the Illinois legislature intended to provide an exemption from sales and use taxes on airline fuel purchased for use on inbound (as well as outbound) international flights when it passed Public Act 86-244, or
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> Whether the legislative changes to the Use Tax Act passed in Public Act 88-547 were substantive changes or clarifications of existing law with respect to the

exemption for airline fuel purchased for international flights.

If either alternative were resolved in favor of the Department, the second issue was whether the penalty assessed as part of NTL no. XXXXX should be abated because TAXPAYER had reasonable cause for failing to pay use tax when due. I am including in the recommendation findings of fact and conclusions of law. I recommend the taxability issue be resolved in favor of the Department, and the penalty be abated.

Findings of Fact:

1. Public Act ("P.A.") 86-244 was titled "AN ACT in relation to use and occupation taxes and air common carriers, amending named Acts."

2. Section 1 of P.A. 86-244 amended section 3 of Illinois' Use Tax Act ("UTA") to provide, in part:

> A tax is imposed upon the privilege of using in this State tangible personal property, . . . other than fuel and petroleum products sold to or used by an air common carrier, certified by the carrier to be used for consumption, shipment or storage in the conduct of its business as an air common carrier, for a flight destined for a destination outside the United States . . . .

P.A. 86-244 (*codified at* Ill. Rev. Stat. ch. 120, ¶ 439.3 (1989)).

3. Public Act 86-244 became effective August 15, 1989.

4. When the Illinois General Assembly passed P.A. 86-244, aircraft fuel withdrawn from warehouses bonded under United States Customs regulations, and loaded for use as supplies or equipment onto vessels (including aircraft) actually engaged in foreign trade was not subjected to federal tax or to import duties (19 U.S.C. §§ 1309, 1317 (1989) (sections relating to import duty and federal tax exemption for supplies for certain vessels and aircraft); 19 U.S.C. 1555-60 (sections relating to bonded warehouses).

5. Bonded fuel was also not subjected to Illinois retailers' occupation tax ("ROT") or to Illinois use tax ("UT"). TAXPAYER Ex. Nos. 1-2; McGoldrick v. Gulf Oil Corp., 309 U.S. 414, 60 S.Ct. 664, 84 L.Ed. 840 (1940) (states pre-

empted from levying excise taxes on fuel withdrawn from customs bonded warehouses for use as equipment or supplies on vessels actually engaged in foreign trade); Itel Containers International Corp. v. Huddleston, 507 U.S. 60, 69-70, 113 S.Ct. 1095, 1102 (1993).[1]

6. Because bonded fuel was not subject to federal tax and duties or to Illinois ROT and/or UT when so used, the price of such bonded fuel was less per barrel than the price of airline fuel refined domestically. *See* TAXPAYER Ex. Nos. 1-2.

7. Prior to the enactment of P.A. 86-244, TAXPAYER had been using (i.e., it withdrew and loaded onto aircraft at O'Hare airport in Chicago) bonded fuel for use or consumption on its flights engaged in foreign trade. *See* Hearing Transcript ("Tr.") pp. 81-82 (testimony of WITNESS ("WITNESS"), TAXPAYER's director of state and local taxes).

8. Shortly after P.A. 86-244 became effective, TAXPAYER received a memorandum from the International Air Transportation Association, an industry group of which TAXPAYER is a member, regarding that legislation. TAXPAYER Ex. No. 6.

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[1]. In Itel, the Supreme Court recently summarized the bases for its holding in McGoldrick over fifty years ago:

> In *McGoldrick* and its progeny, we stated that Congress created a system for bonded warehouses where imports could be stored free of federal customs duties while under the continuous supervision of local customs officials "in order to encourage merchants here and abroad to make use of TAXPAYER ports." [citations omitted] By allowing importers to defer taxes on imported goods for a period of time and to escape taxes altogether on reexported goods, the bonded warehouse system "enabled the importer without any threat of financial loss, to place his goods in domestic markets or to return them to foreign commerce and, by this flexibility encouraged importers to use TAXPAYER facilities." [citations omitted] This federal objective would be frustrated by the imposition of state sales and property taxes on goods not destined for domestic distribution, regardless of whether the taxes themselves discriminated against goods based on their destination. [citations omitted]

Itel, 507 U.S. at 69-70, 113 S.Ct. 1102.

9. After P.A. 86-244 was enacted, TAXPAYER began to purchase domestically refined airline fuel at its O'Hare airport facilities, and it loaded such fuel onto its aircraft for use or consumption on flights in foreign trade. Tr. pp. 83-84 (WITNESS).

10. During the years covered by the NTL's, section 3 of the UTA was resectioned (*see* P.A. 86-1475, eff. January 10, 1991), and the applicable provision codified at section 3-5 of the UTA. Ill. Rev. Stat. ch. 120, ¶ 439.3-5(12) (1991).

11. Shortly after the applicable provision of the UTA was resectioned, the Department adopted a regulation regarding the exemption for international airline fuel. 15 Ill. Reg. 6621, 6647-48 (April 17, 1991).

12. As promulgated, Department rule 130.321 provided:

> Section 130.321 Fuel Used By Air Common Carriers in International Flights
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> (a) Notwithstanding the fact that sales may be at retail, fuel and petroleum products sold to or used by an air common carrier, certified by the carrier to be used for consumption, shipment or storage in the conduct of its business as an air common carrier, for a flight destined for a destination outside the United States is exempt from tax.
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> (b) An air common carrier means a commercial air common carrier certified and authorized to conduct international flights involving passengers or cargo for hire, on a regularly-scheduled basis.
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> (c) Flights destined for a destination outside the United States include flights which originate in Illinois or have a stopover in Illinois and which may have intermediate stops at other locations in the United States prior to arriving at the destination outside the United States. In such situations, all fuel loaded for such a flight shall be considered to be exempt, notwithstanding the fact that a portion of the fuel will be consumed within the United States. If a flight is loaded with exempt fuel for an intended international flight, but for some reason the flight stops at an intermediate location in the United States and does not continue to the foreign destination, the fuel will be taxable.

> (d) In general, exempt international fuel shall be treated in the same manner as bonded fuel with respect to the sale, accountability and eligibility of tax exemptions.
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> (e) Exempt international fuel may be commingled with other jet fuel within the hydrant systems at qualifying airports. However, accurate records must be maintained with respect to the purchaser, gallonage of fuel loaded, flight number, aircraft tail number, ultimate foreign destination and intermediate stops.

86 Ill. Admin. Code § 130.321; 15 Ill. Reg. 6621, 6647-48 (April 17, 1991).

13. After P.A. 86-244 became law, the Department conducted an audit of TAXPAYER's business for a three year period ending 12/31/89. *See* Department Ex. No. 3, pp. 1-2, 6; Tr. pp. 86-88 (WITNESS). The record is unclear whether that prior audit took place before or after Department rule 130.321 was promulgated. TAXPAYER asserts that, during that prior audit, the Department did not assess use tax on its purchases of fuel that it loaded onto aircraft in Chicago for use on flights returning from foreign locations and destined for a destination within the United States. Tr. pp. 87-88 (WITNESS).

14. Public Act 88-547 was entitled, "An Act in relation to taxation", and became effective June 30, 1994. Section 6 of P.A. 88-547 amended the UTA by changing section 3-5 to provide, in part:

> Use of the following tangible personal property is exempt from the tax imposed by this Act:
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> * * *
>
> (12) Fuel and petroleum products sold to or used by an air common carrier, certified by the carrier to be used for consumption, shipment or storage in the conduct of its business as an air common carrier, for a flight destined for or returning from a location or locations outside the United States without regard to previous or subsequent domestic stopovers.

P.A. 88-547 (*codified at* 35 **ILCS** 105/3-5(12) (1994)).

15. The period covered by the audit leading to the NTL's issued in this case was from 1/1/91 through 12/31/93. Department Ex. No. 3, pp. 1, 6. The Department issued NTL no. XXXXX for the period from 1/1/91 through and

including 11/31/93, and NTL no. XXXXX for the period beginning 12/1/93 through 12/31/93. Department Ex. No. 5, pp. 1-2.

16. The total amount of tax assessed in the two NTL's, not counting penalty and interest, was $3,150,940.00. Department Ex. No. 4, pp. 1-3 (total amount of tax identified in NTL's equals the total of the auditor's summary analysis schedule).

17. This dispute involves only part of the total tax identified in the NTL's issued. Department Exhibit Number ("Department Ex. No.") 4, p. 3 (Schedule I, Summary Analysis); Pre-Trial Order; Tr. pp. 10 (Department's opening statement), 107-08 (introduction of Department Ex. No. 4).

18. The total amount of tax at issue is $2,325,675.00, not counting penalty and interest. Department Ex. No. 4, p. 3 (item description "fuel"); Department Ex. No. 3, auditor comments, p. 2; Tr. p. 108.

19. The Department denied TAXPAYER's claim of exemption from use tax regarding certain purchases of fuel after determining that the fuel purchased was loaded onto aircraft whose flights originated outside the United States and which flights were *en route* to a destination within the United States. Department Ex. No. 3, p. 2. TAXPAYER loaded the fuel onto such aircraft during stopovers at O'Hare airport, in Chicago, Illinois. *Id.*

20. TAXPAYER did not dispute the accuracy of the auditor's identification of intended international flights whose journeys were cancelled due to mechanical problems after fuel was purchased in Illinois. Pre-Trial Order; *see also* Department Ex. No. 4, p. 3 (item description "fuel canc", audit code no. "62-107"); 86 Ill. Admin. Code § 130.321(c). TAXPAYER did not protest the tax assessed on its use of such fuel in this case. Pre-Trial Order.

21. The legislative history regarding P.A. 86-244 is detailed, or is referred to, in the following public documents: Index to the Transcripts of the House Debates of the 86th General Assembly [hereinafter "Index to 86th G.A. House

Transcripts"] 142 (May 1991); Index to the Transcripts of the Senate Debates of the 86th General Assembly [hereinafter "Index to 86th G.A. Senate Transcripts"] 72 (January 1989 - January 1991); Final Legislative Synopsis and Digest of the 1989 Session of the 86th General Assembly, State of Illinois (No. 17, Vol. 3) [hereinafter "1989 Final Legis. Digest"] 1818.[2]

22. The legislative history regarding P.A. 88-547 is detailed, or is referred to, in the following public documents: Final Legislative Synopsis and Digest of the 1994 Session of the 88th General Assembly, State of Illinois (No. 12, Vol. 1) [hereinafter "1994 Final Legis. Digest"] 687-89; Index to the Transcripts of the House Debates of the 88th General Assembly [hereinafter "Index to 88th G.A. House Transcripts"] 299-300 (January 13, 1993 - January 10, 1995); Index to the Transcripts of the Senate Debates of the 88th General Assembly [hereinafter "Index to 88th G.A. Senate Transcripts"] 167 (January 13, 1993 - January 10, 1995) (microfiched transcripts of debates available at the Illinois Attorney General's library in Chicago); *see also* Journal of the Senate of the 88th General Assembly of the State of Illinois (1994 Session) (various pages recount the text of bill as filed, the text of amendments thereto, and the results of votes taken at each step).

Conclusions of Law:

This dispute involves TAXPAYER's purchases and use of fuel during the period after P.A. 86-244 was enacted and before that Act was amended by P.A. 88-547. The text of P.A. 86-244 created an exemption for fuel loaded onto an air common carrier's aircraft and used, consumed or stored on "a flight destined for a destination outside the United States." The text of P.A. 88-547 applies the exemption to fuel loaded onto such aircraft for use . . . "for a flight destined for or returning from a location or locations outside the United States without

[2]. I take note of the legislative history regarding P.A. 86-244 and P.A. 88-547, the two Acts whose interpretation the parties agreed were part of the issues in this matter.

regard to previous or subsequent domestic stopovers either inbound or outbound international flights."

The parties submitted that the issue presented at hearing could be resolved by answering one of two alternative statements of the issue. Pre-Trial Order. The parties' alternative statements of the issue are corollaries of one another. For example, if the General Assembly intended the exemption to apply to fuel loaded onto aircraft and used, consumed or stored on either inbound or outbound international flights, then the 1994 changes to section 3-5 of the UTA must have merely clarified what the legislature intended to do through P.A. 86-244 in 1989. If, however, P.A. 88-547 was meant to change the effect of P.A. 86-244, then the General Assembly must have originally intended the exemption created by that Act to not apply to purchases of fuel loaded onto an air common carrier's aircraft whose flights were destined for a destination inside the United States. Although the parties seem to have agreed that only one of the issue statements need be answered, I will address them both.

The parties do not dispute the facts otherwise necessary to claim the exemption. For example, the parties do not dispute that TAXPAYER was an air common carrier. Nor do they dispute that the fuel purchased was certified by TAXPAYER to be used for consumption, shipment or storage in the conduct of TAXPAYER's business as an air common carrier. *See* Pre-Trial Order. The Department's auditor reviewed TAXPAYER's books and records, and determined that TAXPAYER loaded, in Illinois, a certain amount of fuel onto aircraft whose flights originated at locations outside the United States, and whose flights terminated elsewhere within the United States after a stopover in Illinois. Department Ex. No. 3, pp. 2, 8; Department Ex. No. 4, p. 3. The parties agreed that the major dispute is limited to purely legal questions of legislative intent. *See* Pre-Hearing Order.

The primary source for ascertaining the General Assembly's intent is the text of the statute itself. *See, e.g.*, Carver v. Bond/Fayette/Effingham Regional

Bd. of School Trustees, 146 Ill. 2d 347, 353, 586 N.E. 2d 1273, 1275 (1992); Kraft v. Edgar, 138 Ill. 2d 191 (1990). The Department argues the text of P.A. 86-244 is clear and unambiguous. Because TAXPAYER loaded the fuel at issue onto aircraft whose flights originated outside the United States and terminated within the United States, the exemption does not apply to TAXPAYER's use of fuel here. The Department argues that when the legislature provides a tax exemption for fuel used by air common carriers for flights "destined for a destination *outside* the United States", the provision cannot be understood to apply to fuel used for flights destined for a destination *inside* the United States. *See* Department's Response To Taxpayer's Post-Trial Brief ("Department's Response"), pp. 5-6.

TAXPAYER claims the General Assembly always intended the exemption for airline fuel to be applied in a manner coextensive with the federal and Illinois exemptions afforded airline fuel withdrawn from bonded customs warehouses. TAXPAYER argues that the Department's own regulation provides that the Illinois exemption shall be treated in the same manner as bonded fuel. Since the exemption afforded bonded fuel applies to fuel loaded onto aircraft engaged both ways in foreign commerce (i.e., aircraft whose flights originate in foreign countries and terminate within the United States and aircraft whose flights originate in the United States and terminate in foreign countries), the Illinois exemption should apply to fuel loaded onto inbound and outbound international flights as well. *See* TAXPAYER Airline's Trial Brief ("TAXPAYER's Brief"), pp 1-2.

At hearing, both parties focused their arguments primarily on the text or the history of P.A. 86-244. The only evidence introduced regarding the legislative history of P.A. 86-244 was introduced by TAXPAYER. That evidence consists of a transcript of an Illinois House of Representatives revenue subcommittee meeting held on 4/26/89. TAXPAYER Ex. No. 2. Neither party offered any evidence regarding the legislative history surrounding the passage of P.A. 88-547, although the question of whether a subsequent amendment to a statute clarified or changed existing law similarly calls into question legislative

intent. *See e.g.*, Rivard v. Chicago Fire Fighters Union, 122 Ill. 2d 303, 308-09 (1988) (Illinois Supreme Court reviewed principals governing its interpretation of statutes with regard to their prospective or retroactive operation).

During pre-trial status conferences in this matter, the parties advised that they had searched for legislative history regarding P.A. 86-244, with little success. I have also reviewed the public record for history of the legislation with little substantive results. *See* Index to 86th G.A. House Transcripts 142 (refers to single entry of April 7, 1989, the date of the bill's first reading in the House); Index to 86th G.A. Senate Transcripts 72; 1989 Final Legis. Digest 1818.[3] The transcript of the revenue subcommittee meeting, however, provides some insight regarding the circumstances existing when HB 2209 was being considered by the Illinois General Assembly.

House Bill 2209 was initiated through the efforts of domestic refiners of airline fuel and/or petroleum products. *See* TAXPAYER Ex. No. 1 (memo produced by a Shell Oil Co. employee for distribution to the Illinois legislature regarding HB 2209); TAXPAYER Ex. No. 2, pp. 1-2 (representatives of Shell Oil Co., Amoco, and Marathon Oil Co. present at the revenue subcommittee conference); Tr. pp. 23-26 (testimony of Kenneth Spaulding). The "evil" those domestic refiners and retailers sought to remedy through legislation was the asserted competitive advantage enjoyed by airline fuel produced outside the United States and brought into the United States through pipelines and storage facilities under the authority of the United States Customs Service. *See* TAXPAYER Ex. Nos. 1-2.

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[3]. House Bill 2209 was placed on a consent calendar in the House. 1989 Final Legis. Digest 1818. No substantive discussion of the bill appears in the transcript during the first reading of HB 2209 in the House (*see* 86th Ill. Gen. Ass., House of Representatives Transcription Debate, April 7, 1989, p. 13), or in the transcripts during the three readings of HB 2209 in the Senate. Index to 86th G.A. Senate Transcripts 72; 86th Ill. Gen. Ass., Senate Transcripts for: May 25, 1989, p. 9; June 15, 1989, pp. 6-7; June 19, 1989, p. 166 (respectively, the first, second and third readings of the bill in the Senate).

The last entry contained in the Index to the Senate Transcripts regarding HB 2209 appears to be in error. *See* Index to 86th G.A. Senate Transcripts 72. My search of the Senate transcripts revealed no legislative activities for July 27, 1989.

Since fuel withdrawn from bonded customs warehouses and used as equipment or supplies on vessels in foreign trade was not subjected to federal tax or to import duties (*see* 19 U.S.C. §§ 1309, 1317; 19 C.F.R. § 10.59), or to Illinois excise taxes (*see* McGoldrick v. Gulf Oil Corp., 309 U.S. 414, 60 S.Ct. 664, 84 L.Ed. 840 (1940)), the price of bonded fuel was less per barrel than the price of airline fuel sold by the Illinois refiners. *See* TAXPAYER Ex. Nos. 1-2. The Illinois petroleum refining and retailing industry wanted HB 2209 passed so they could substitute the products they refined and sold domestically for the fuel then being purchased by local air common carriers for use or consumption on aircraft during flights in foreign trade, by making the sales of such domestically-produced airline fuel exempt from Illinois ROT.

The sellers of domestically refined petroleum products might well have publicly proclaimed that P.A. 86-244 eliminated the need for air common carriers to make purchases of bonded fuel, and encouraged such carriers to freely substitute domestically refined airline fuel for the bonded fuel they had been purchasing. That, in fact, is what TAXPAYER admittedly did here. TAXPAYER's Brief, pp. 7-8. From the domestic petroleum manufacturer's perspective, P.A. 86-244 created a considerable local market for domestically-refined fuel, while avoiding most, if not all, of the transaction costs associated with substantiating the deductions from taxable gross receipts,[4] or with the other costs of compliance with the strictly controlled conditions that existed under applicable Treasury regulations. *See, e.g.* 19 C.F.R. § 10.60 (principal or authorized designee must sign for withdrawal fuel from a bonded warehouse); 19

[4]. The text of P.A. 86-244 implies the nature of the documentation a retailer would be required to maintain and produce for inspection or audit to support the deduction from the retailers' taxable gross receipts. *See* Hess, Inc. v. Department of Revenue, 278 Ill. App. 3d 483 (5th Dist. 1996). Here, that documentation would likely consist of a regularly updated blanket exemption certificate, signed by the air common carrier, on which the carrier certified that all purchases of airline fuel made after the date on the certificate were being purchased for consumption, shipment or storage on flights destined for a destination outside the United States.

C.F.R. § 10.62(a) (forms required to make withdrawal of fuel from bonded warehouse); 19 C.F.R. § 10.62(f) (Customs has right to inspect records to be kept by withdrawers, deliverers and receivers of fuel) (1990).

The revenue subcommittee transcript introduced by TAXPAYER reflects what the domestic petroleum refiners desired when seeking passage of HB 2209. Those industry sponsor's statements at that subcommittee meeting should not be considered in the same light as the statements of the elected officials during Illinois House or Senate debates. Illinois Federation of Teachers v. IELRB, 278 Ill. App. 3d 954, 959 (1st Dist. 1996). It is more likely, as the Department has pointed out, that the General Assembly gave the interested parties part, but not all, of what they asked for. *See* Department's Response, p. 7. For example, the industry spokesman told the House revenue subcommittee that "[w]e [the retailers of domestically-refined petroleum products] would like to have the domestic fuel sold under those controlled conditions be exempt as well" (*see* TAXPAYER Ex. No. 2, p. 2), but P.A. 86-244 did not propose to institute any system of controls similar to the controls placed on the persons who imported and stored fuel in customs bonded warehouses.

Nor did the Illinois General Assembly use terms in P.A. 86-244 that were clearly traceable to terms found within the federal statutes and customs regulations affecting bonded fuel, or expressly refer to any applicable federal provisions in the text of P.A. 86-244. *See, e.g.* 19 U.S.C. §§ 1309(a)(1)(C), 1309(a)(3) (federal import duty and tax exemptions extended to supplies and equipment stored in bonded warehouse and withdrawn for use on vessels "actually engaged in foreign trade"); 19 C.F.R. § 10.59(a) ("actually engaged in foreign trade" defined); TAXPAYER Ex. No. 3 (Treasury decisions holding that equipment and supplies loaded onto aircraft during scheduled stopovers but before flights reached intended destinations would not be subject to federal import duties. Those decisions held that the carriers were still actually engaged in "foreign trade" within the meaning of section 309(a)(c) of the Tariff Act of 1930.). The

considerable differences between the text of P.A. 86-244 and the texts of the federal statutes and customs regulations governing the tariff and tax exemptions granted bonded fuel make it unlikely the General Assembly intended the scope of the Illinois exemption to be identically coextensive with the scope of those federal exemptions. *Compare* P. A. 86-244 *with* 19 U.S.C. §§ 1309 (supplies for certain vessels and aircraft); 19 U.S.C. 1555-60 (sections relating to bonded warehouses) *and* 19 C.F.R. §§ 10.59-10.64.

Another source for ascertaining legislative intent is the agency's interpretation of the statute it is charged with administering. Dover Corp. v. Department of Revenue, 271 Ill. App. 3d 700, 705 (1st Dist. 1995). TAXPAYER argues it relied on subparagraph (d) of Department rule 130.321 to its detriment. TAXPAYER's Brief, p. 13. TAXPAYER argues the Department knew the exemption for bonded fuel applied to fuel used on inbound international flights, i.e., flights destined for a destination *inside* the United States. *Id.*, p. 10; TAXPAYER's Reply, p. 14; *but see* Department's Response, pp. 13-16 & n.4. I agree with TAXPAYER that when the Department wrote that Illinois' exemption for international fuel "[i]n general, . . . shall be treated in the same manner as bonded fuel with respect to the sale, accountability, and eligibility of tax exemption", it should have known which withdrawals from bonded warehouses were eligible for exemption under federal law. *See* TAXPAYER's Reply, p. 14. The Department could hardly treat exempt international fuel in the same manner as bonded fuel without knowing how eligibility was determined for the federal duty and tax exemptions afforded bonded fuel. Therefore, I will presume the Department knew of the general eligibility for exemptions from import duties and taxes afforded fuel kept in customs bonded warehouses when it promulgated rule 130.321.

But accepting TAXPAYER's argument on that point does not resolve whether the Department's regulation reflects the General Assembly's intent to have P.A. 86-244 apply to fuel loaded onto aircraft for flights destined for a destination

inside the United States. Regulations, like statues, must be read so that no provision is rendered superfluous or meaningless. Kraft v. Edgar, 138 Ill. 2d 191 (1990). Here, paragraph (d) of rule 321 must be read together with paragraph (c), and with the other parts of the rule. Paragraph (d), it should be remembered, begins with words of qualification -- "*[i]n general*, exempt international fuel shall be treated in the same manner as bonded fuel . . . ." 86 Ill. Admin. Code § 130.321(d) (emphasis added). TAXPAYER's reading of paragraph (d) renders meaningless paragraph (c) of that rule, in which the Department interpreted P.A. 86-244's statutory phrase "flight[s] destined for a destination outside the United States." And the two paragraphs need not be read in conflict. If inconsistency is to be avoided, paragraph (c) should be read as the articulated exception to the general rule set forth in paragraph (d).

In paragraph (c) of its regulation, the Department interpreted the statutory phrase "flight[s] destined for a destination outside the United States" to include:

> flights which originate in Illinois and which may have intermediate stops at other locations in the United States prior to arriving at the destination outside the United States, and
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> flights which have a stopover in Illinois and which may have intermediate stops at other locations in the United States prior to arriving at the destination outside the United States.

86 Ill. Admin. Code § 130.321(c). The Department's regulatory interpretation of the statutory phrase was consistent with the common, ordinary meaning of the words used in P.A. 86-244,[5] and that interpretation neither extended the Department's authority nor imposed a limitation on the exemption as written. *See, e.g.*, Wesko Plating v. Department of Revenue, 222 Ill. App. 3d 422, 425-26 (1st Dist. 1991).

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[5]. The term "destination" means "The place to which someone or something is going." The TAXPAYER Heritage Dictionary 387 (2d ed. 1985). "Destine" is defined as "To determine beforehand; preordain. . . . To direct toward a given destination: *a flight destined for Tokyo*." *Id.* (emphasis original)

The uses not identified within the Department's interpretation of the phrase "flight[s] destined for a destination outside the United States" must be understood as having been excluded from the Department's interpretation of that phrase. Subparagraph (c) gave notice to all persons, including all refiners of domestic petroleum products and all air common carrier purchasers of such products, that fuel used, consumed or stored on flights which were not, either by design or by happenstance, "destined for a destination outside the United States" remained subject to ROT and UT. On this point, TAXPAYER does not challenge the use tax imposed because of the effect of the second sentence in Department rule 321(c). *See* Department Ex. No. 3, p. 2; Department Ex. No. 4, p. 3 (item description "fuel canc", audit code no. "62-107"); Pre-Trial Order.

Giving full meaning to the whole of paragraph (c) is also consistent with paragraph (e)'s direction that accurate records be maintained with respect to, *inter alia*, the "ultimate *foreign* destination" of the flights onto which fuel was loaded. 86 Ill. Admin. Code § 130.321(e) (emphasis added). If the Department interpreted the exemption to apply to fuel loaded onto both inbound and outbound international flights, the word "foreign" in paragraph (e) would also be rendered meaningless.

I cannot conclude that the Department's regulation reflected either the Department's or the legislature's intent to make the exemption created by P.A. 86-244 applicable to fuel loaded onto flights destined for a destination inside the United States. There is insufficient evidence in the record adduced at hearing, or in the legislative history of record regarding HB 2209, to support the conclusion that the Illinois General Assembly intended the scope of the exemption created by P.A. 86-244 to be identically coextensive with the federal tax and duty exemptions granted fuel stored in customs bonded warehouses.

Compared to P.A. 86-244, there is a wealth of legislative history regarding P.A. 88-547. Specifically, there is history regarding whether the General Assembly intended that Act to be applicable prospectively or retroactively.

Before I detail that history, I will identify some of the principals the Illinois Supreme Court has declared should be considered when determining whether an amendment to an act is to be given retroactive or prospective application. "Generally, a material change in the language of an unambiguous statute creates a presumption, although it can be rebutted by evidence of a contrary legislative intent, that the amendment was intended to change the law." State of Illinois v. Mikusch, 138 Ill. 2d 242, 252 (1990).[6] In cases where a later amendment to a statute has been construed as a clarification rather than a change in law, some ambiguity existed in the statute prior to the amendment. *Id.* If circumstances suggest the legislature intended to interpret, or clarify the original statute, the presumption of change is rebutted. Jacobson v. General Finance Corp, 227 Ill. App. 3d at 1097; Hyatt Corp. v. Sweet, 230 Ill. App. 3d 423, 429 (1st Dist. 1992). Under such circumstances, "[t]he presumption of prospectivity is rebuttable, but only by the act itself. *Either by express language or necessary*

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[6] Prior to hearing, I indicated the language of P.A. 86-244 was ambiguous, i.e., that it was capable of being understood in more than one way by reasonable people. In its post-hearing memorandum, the Department asked that I reconsider that determination of ambiguity. Department's Response, p. 6 & n.2. When reviewing the transcript and record of the proceedings in this case with the benefit of hindsight, the Department may well be correct when it argues that any ambiguity may have been caused more by the text of the Department's regulation vis-a-vis the issues to be resolved, than by the text of P.A. 86-244. Specifically, the Department's argument that the exemption did not apply to inbound international flights is, at first blush, inconsistent with its own regulatory interpretation of the statutory phrase "flight[s] destined for a destination outside the United States" in subparagraph (c) of rule 130.321. *See* Department's Response, p. 16 & n.4. Under the Department's own rule, *some* inbound international flights would still meet the definition of a flight "destined for a destination outside the United States." A simple example might be a flight originating in London with a scheduled stop in Chicago, that took on fuel during the Illinois stopover, and which then continued toward its destination in Mexico City.

With regard to the Department's request that I reconsider my conclusion regarding the ambiguity of P.A. 86-244, even if it was erroneous, it is entitled to no deference, either by the Director or by a reviewing court. *See, e.g.* Branson v. Department of Revenue, 168 Ill. 2d 247 (1995) (proper interpretation of ROTA's provisions is a question of law subject to *de novo* review); Hyatt Corp. v. Sweet, 230 Ill. App. 3d 423, 429 (1st Dist. 1992) (reviewing court not bound by parties' agreement regarding clarity of statutory provision, nor with circuit court's conclusion that text of a statute was ambiguous); 86 Ill. Admin. Code § 200.165 (1996) (recommended decision may be rejected in whole or in part by Director or his designee).

implication, the act must clearly indicate that the legislature intended a retroactive application." Rivard v. Chicago Fire Fighters Union, 122 Ill. 2d 303, 309 (1988) (emphasis added).

Consistent with the Supreme Court's rule in Rivard, in cases where it was determined that an amendment merely clarified an existing statutory provision, courts have identified the General Assembly's intent by citing to the legislative history of the amendatory act itself. For example, in Falato v. Teachers Retirement Systems, 209 Ill. App. 3d 419, 425 (1st Dist. 1991), the First District reviewed legislative history regarding an amendment to the definition of the term "teacher" in sections of the Illinois Pension Code. Because that history supported a determination that the amendment was intended to clarify existing law, the court held that the amendment should be applied retroactively. Falato, 209 Ill. App. 3d at 425. Similarly, in Hyatt Corp. v. Sweet, the court found that the legislative history regarding an amendment to section 2e of the ROTA supported its determination that the amendment was intended to clarify -- and not to change -- existing law. Hyatt Corp. v. Sweet, 230 Ill. App. 3d 423, 434-37. There is no such clear intent found in the legislative history of record for P.A. 88-547.

Public Act 88-547 began as Senate Bill ("SB") 1691. Senator DeAngelis, the original sponsor of SB 1691, filed the bill on March 4, 1994. 1994 Final Legis. Digest 688. As filed, SB 1691 proposed to amend the Illinois Income Tax Act to extend the sunset date for a research and development tax credit ("R&D credit") scheduled to expire on 12/31/94. ***Id.*** The first two amendments filed regarding SB 1691 proposed, respectively: (1) to amend the ROTA to provide an exemption for tangible personal property sold and delivered to a common carrier by motor who then transports the property outside Illinois; and (2) to amend the Illinois Income Tax Act to eliminate the requirement that the Department evaluate the effect of the income tax R&D credit and report its findings to the General

Assembly. 1994 Final Legis. Digest 687; Journal of the Illinois Senate (March 24, 1994) 389-90 (text of amendments as filed).

On April 11, 1994, Senator DeAngelis filed Senate Amendment 3 to SB 1691. 1994 Final Legis. Digest 688. Senate Amendment 3 proposed to amend, *inter alia*, the use tax act's exemption for airline fuel to include substantially the same text that currently appears in section 3-5(12) of the UTA. Journal of the Illinois Senate (April 14, 1994) 652-56 (text of amendment 3). On April 14, 1994, Senator DeAngelis offered the following explanation regarding amendment 3 to SB 1691:

> **Senator DeAngelis:**
> Thank you, Madam Chairman. Amendment No. 3 to Senate Bill 1691 exempts from Illinois taxes jet fuel used on domestic segments of inbound international flights. Currently such fuel is exempt from federal taxation. *This is the only instance where the State tax treatment of airline fuel differs from federal tax treatment.* So essentially what happens in this particular instance, the airlines are forced to buy offshore fuel from nondomestic producers and put it in a bonded situation to avoid the tax. *This bill is revenue-neutral because -- this amendment is revenue-neutral because they're not buying that gas domestically anyhow. What it would do, it would allow them to buy it domestically and use our current sources and use that in those segments of international flights in which they land in Chicago.* Be happy to answer any questions.

88th Ill. Gen. Ass., Senate Proceedings (Transcript), April 14, 1994, pp. 103-04 (emphasis added). Senate Amendment 3 was adopted by the Senate on April 14, 1994. *Id.*, p. 104; 1994 Final Legis. Digest 688.

At the third reading of SB 1691, Senator DeAngelis said:

> **Senator DeAngelis:**
> Thank you, Mr. President. As all of know, there has been in effect in Illinois for five years an income tax credit for research and development. It was due to sunset this year. This bill extends the sunset to the year 1999. *As amended, it allows the exemption of fuel -- jet fuel -- used on domestic flights on inbound international flights. This is prospective. It is revenue-neutral because, currently, such fuel is exempt from federal taxation. And if we do not pass this, what it does, it allows these carriers or, in fact, forces them to buy foreign fuel, put it in the tank, and it's called bonded fuel. This bill*

> *then -- now would allow us to purchase domestic fuel and be on a parity in taxation, as they are everyplace else.*

88th Ill. Gen. Ass., Senate Proceedings (Transcript), April 21, 1994, pp. 186-87 (emphasis added).

Senator DeAngelis' statements do not support TAXPAYER's argument that SB 1691 was introduced to clarify the General Assembly's original intent behind P.A. 86-244. Senator DeAngelis' first debate statements reflect the sponsor's recognition that, in 1994, the Illinois exemption for airline fuel *differed* from the federal exemption granted to air common carriers purchasing bonded fuel. 88th Ill. Gen. Ass., Senate Proceedings (Transcript), April 14, 1994, pp. 103-04. The Senator also remarked (mistakenly, as this case proves) that air carriers were not buying domestically refined fuel for inbound flights because of the difference between the federal exemption and the Illinois exemption. But the Senator's mistake of fact does not change the rationality of his assumption regarding the market's behavior in response to the current state of the law. If a willing customer has the choice of making a purchase of equally conforming goods, one type being subject to tax (thereby raising the cost of the goods to the purchaser) and the other type not being subject to tax, the purchaser will be more likely to buy the untaxed goods.

Had the senator believed the exemption passed via P.A. 86-244 was originally intended to apply to fuel loaded onto aircraft on flights originating at a foreign port and destined for a destination inside the United States, he would not have stated that the Illinois exemption differed from the federal exemptions in precisely that respect. Instead, his remarks reflect an understanding of Illinois law that mirrors the Department's arguments at hearing. After P.A. 86-244 was passed, and before it was amended, fuel loaded onto aircraft for flights destined for a destination *outside* the United States was exempt from Illinois use tax, but fuel loaded onto aircraft on a stopover in Illinois during a flight originating outside the United States and destined for a destination *inside* the United States was not exempt.

The highlighted portions of Senator DeAngelis' statements at the third reading of SB 1691 also reflect an intent to change existing law. First, the senate sponsor clearly articulated that the bill was meant to have prospective, and not retroactive, effect. 88th Ill. Gen. Ass., Senate Proceedings (Transcript), April 21, 1994, pp. 186-87. More importantly, the senate sponsor repeated his understanding that under then-current Illinois law, fuel purchased by an air common carrier and loaded onto its aircraft during an Illinois stopover of an inbound international flight whose destination was inside the United States *would* be subject to Illinois use tax, *unless* the fuel being purchased was bonded fuel. *Id.*

After being adopted by the Senate, SB 1691 moved to the Illinois House of Representatives. 1994 Final Legis. Digest 688. When the bill was called for the third reading in the House, Representative Novak made the following presentation:

> **[Representative] Novak:**
> Yes, Mr. Speaker, Ladies and Gentlemen of the House. Senate Bill 1691 is a very important measure that the Illinois business community needs to continue. What the underlying Bill essentially does, it extends the research and development tax credit that is about to sunset at the end of this year. It extends it, for I believe, for two more years. Studies done by the Department of Revenue indicate that this research and development tax credit that is utilized by Illinois businesses creates a real and tangibly beneficial effect. It creates jobs. And this is born[e] out by studies and analyses done by the Department of Revenue. The Department of Revenue is certainly behind this legislation as well as the entire business community. It's a very important piece of legislation to keep . . . to let us . . . to allow us to continue the research and development tax credit. *Also on the Bill, there are some provisions dealing with some clean-up language for the airline fuel industry because of some of the differences in the language, number of years ago, dealing with whether plane . . . when planes take off and they go overseas, about tax credits or tax exemptions that are given by foreign countries on intercontinental flights in relation to flights that are in truck, [sic] continental within the borders of the United States.* And this was also agreed to by all the parties. So be more than happy to entertain any questions. This bill should have passed the House, now goes back to the Senate for concurrence and then to the Governor's office.

88th Ill. Gen. Ass., House of Representatives Transcription Debate, June 9, 1994, p. 124 (emphasis added; ellipses original).

To be fair, it is possible that when the representative uttered the words "clean-up language" he meant "clean-up" to be synonymous with "clarifying". *See, e.g.*, City Suburban Electric Motors v. Wagner, 278 Ill. App. 3d 564, 568 (1st Dist. 1996). But when compared to the more focused, specific and repeated statements of Senator DeAngelis -- the original sponsor of SB 1691 -- the representative's debate is just too weak a foundation upon which to base a conclusion that SB 1691 was meant to clarify the law as it existed under P.A. 86-244.

Although the parties dispute whether a controversy existed regarding the interpretation of P.A. 86-244 prior to the introduction of SB 1691 (*see* Department's Response, pp. 10-12; TAXPAYER's Reply, pp. 11-13), I am not convinced that the existence of a controversy, or the date when that controversy might have arisen, are facts that must be found to exist when determining whether the legislature intended an amendatory act to clarify or change existing law. *See* Falato v. Teachers Retirement Systems, 209 Ill. App. 3d at 425. The best evidence that the legislature intended an amendment to apply retroactively is the text of the amendment itself. *See, e.g.*, General Telephone Co. v. Johnson, 103 Ill. 2d 363, 376-77 (1984). There is no such intent expressed in the text of P.A. 88-547. Even if there had been a controversy, the legislative history of P.A. 88-547 corroborates the presumption that that amendatory act was meant to change existing law. Therefore, I cannot recommend that P.A. 88-547 be applied retroactively.

Finally, TAXPAYER protested the Department's assessment of penalties. TAXPAYER argues that penalties should not be assessed here because the Department had not assessed use tax on its purchases of domestically-refined airline fuel for use on inbound international flights during an audit immediately preceding the audit at issue here. Tr. p. pp. 84-88; TAXPAYER's Brief, pp. 8, 18 & n.32.

The Department argues that even if it failed to assess use tax during a prior audit, a penalty should still be assessed from the period following August 20, 1992, the date the Department issued a private letter ruling to another air common carrier in which a Department employee wrote that the exemption was not applicable to fuel loaded onto aircraft for flights destined for a destination inside the United States. Department's Response, p. 20.

I do not agree that the Department's issuance of PLR 92-0436 put TAXPAYER, or the airline industry, on notice that the Department considered fuel used on inbound international flights taxable. *See id.*; *see also* 2 Ill. Admin. Code § 1200.110(a) ("Private letter rulings are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation."). Rule 130.321 should have done that on the date it was promulgated. *See* TAXPAYER's Reply, p. 18.

TAXPAYER's reasonable cause argument is based, in part, on its assertion that its understanding of the exemption was reasonable because the Department did not assess tax on TAXPAYER's use of fuel in the same manner at issue here during a prior audit period, a part of which audit period was after the effective date of P.A. 86-244. The Department auditor's comments do not rebut WITNESS's testimony regarding the Department's prior audit of TAXPAYER. *Compare* Tr. pp. 86-89 (WITNESS) *with* Department Ex. No. 3. The Department's alleged decision not to assess use tax on TAXPAYER's purchases of fuel loaded onto inbound international flights during a prior audit does not estop the Department from arguing that tax is due here. But it does present a sound factual basis for TAXPAYER to claim that it exercised ordinary business care and prudence when it failed to report the same type of purchases as being subject to use tax on returns filed during the following audit period.

In addition to its asserted reliance on the Department's treatment of the same transactions during the immediately preceding audit, TAXPAYER also introduced a memorandum it received from the International Air Transportation

Association ("IATA"), an industry group of which TAXPAYER is a member, at or about the time P.A. 86-244 was enacted into law. TAXPAYER Ex. No. 6. Referring to a letter from the Director of Legal Services for the IATA, the notice provides that, "effective 15 August 1989, fuel and petroleum products sold to or used by airlines for international flights are exempt from the Illinois state retailers' occupation, use and service tax."

I conclude that TAXPAYER has shown, with books and records it retained in the ordinary course of its business, and through the records of the Department which referred to the Department's prior audit of TAXPAYER, that it made a good faith effort to determine and file its proper use tax liability by exercising ordinary business care and prudence. *See* 86 Ill. Admin. Code § 700.400(c) (1994) ("A determination of whether a taxpayer exercised ordinary business care and prudence is dependent upon the clarity of the law or its interpretation and the taxpayer's experience, knowledge, and education."). TAXPAYER rebutted the *prima facie* correctness of the Department's determination that late payment penalties were due.

Conclusion

TAXPAYER has not rebutted the Department's *prima facie* showing that use tax is due on the transactions at issue. There is insufficient evidence in the record adduced at hearing, or to be found in the legislative history of record regarding P.A. 86-244, that the Illinois General Assembly intended the exemption created by that Act to be equally applicable to fuel loaded onto an air common carrier's aircraft for flights destined for a destination outside the United States and to fuel loaded onto an air common carrier's aircraft for flights destined for a destination inside the United States. The legislative history of record also reflects that the Illinois General Assembly intended that P.A. 88-547 change Illinois law, and that it have prospective application. Therefore, P.A. 88-547 should not be applied retroactively here.

I recommend the Director revise Notice of Tax Liability no. XXXXX to eliminate the penalties attributable to TAXPAYER's failure to pay use tax when due on the transactions at issue. I recommend that that notice be finalized as revised, with interest to accrue pursuant to statute. I recommend that Notice of Tax Liability no. XXXXX be finalized as issued, interest to accrue pursuant to statute, and that no late payment penalty be assessed as part of the final assessment.

Date Administrative Law Judge